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RUCPDOG/DEPT OF COMMERCE WASHINGTON DC
RUMICEA/USCENTCOM INTEL CEN MACDILL AFB FL
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RUEHKP/AMCONSUL KARACHI 0760
RUEHLH/AMCONSUL LAHORE 6491
RUEHPW/AMCONSUL PESHAWAR 5348
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SUBJECT: IMF LOOKS FOR USG SUPPORT WITH PROGRAM IMPLEMENTATION

REF: ISLAMABAD 03776

1. (SBU) SUMMARY. EconCounselor met with the IMF's Resident Representative to discuss Pakistan's implementation of economic stabilization policies. They agreed that the SBA adjustment measures are necessary for a stable economy and this message should be continually reinforced with officials of the Government of Pakistan (GOP). The USG and GOP have discussed holding a donors' conference on January 8 in Beijing, a date that could strike the balance between promptly endorsing progress while still achieving a successful conference. The GOP still faces the difficulty of removing the costly electricity subsidies and the trading restrictions on the stock exchange. In February the IMF evaluation team will visit Pakistan for the first assessment of Pakistan's benchmarks. END SUMMARY.

2. (SBU) On December 8, EconCounselor and EconOff met with Paul Ross, the International Monetary Fund's (IMF) Resident Representative in Pakistan to discuss Pakistan's implementation of the Stand-By Agreement (SBA) the IMF board approved November 24. Ross commented that in the past, Pakistan has not always followed through on IMF program commitments, leading to curtailed programs and indicated that the IMF would appreciate additional U.S. reinforcement on the importance of meeting the benchmarks when meeting with GOP officials. While Ross and EconCounselor agreed that it is important to reinforce the message when communicating with the GOP that the SBA adjustment measures are necessary for a stable economy, both also agree that the current quarter will be especially critical for the program as donors will be looking at benchmark commitments as well. Ross noted that Mohsin Khan, Director for Middle East and Central Asia will be visiting Pakistan next week for meetings and the IMF evaluation team will visit Pakistan in February to determine if the program requirements are being met, but the exact date for the team visit has yet to be determined.

DONOR FUNDING IS EXPECTED BUT HAS NOT MATERIALIZED

4. (SBU) EconCounselor said the USG and GOP have discussed holding a donors' conference on January 8 in Beijing but the dates have yet to be finalized. EconCounselor explained that while donors are interested in a prompt response to endorse the GOP's adjustment plan

and the SBA -- and the USG in particular wants to avoid losing the momentum and hold the conference soon to reinforce the program - donors are also interested in seeing that SBA benchmarks are met and that sufficient resources are marshaled to have a successful conference.

15. (SBU) EconCounselor noted that given the global financial crisis, several potential donors are very interested in the results of the GOP's prioritization of development projects as it may be easier to garner support for projects versus direct budgetary support. For example, the USG is acutely aware of the imminent shortage of wheat in Pakistan during this winter and is working to help finance imports from the United States. (reftel)

16. (SBU) Ross noted that the GOP expects China to deposit USD 500 million in Chinese U.S. dollar reserves into the State Bank of Pakistan. The GOP will be permitted to use the reserves for any purpose, including budgetary expenditures, but will then return the reserves to China. China's original offer was at the London interbank lending rate (LIBOR) (2.795 percent as of December 8) plus one percent for a term of one year, but the GOP requested a longer term. This request is being considered but the reserve deposit is expected to be disbursed in December.

17. (SBU) The SBA includes a forecast USD 3.8 billion in financing from the World Bank and Asian Development Bank in fiscal year 2008/2009. However, both banks have had difficulty disbursing and Ross sought USG assistance in trying to press for quick disbursement. Ross noted that, without these funds, meeting quarterly targets will be "very tricky."

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POLICY INTEREST RATE INCREASE

18. (SBU) Ross said that the proposed January increase in the policy rate from 15 percent to 16.5 percent is still under discussion. The decision will be a function of rupee exchange rates, foreign exchange reserve levels, T-bill auction results, and inflation rates. Ross noted that the core inflation rate continued to accelerate for the October figures, so he was interested to see the November rates. He also noted that the policy rate decision will be made factoring in economic indicator data from multiple months.

STOCK EXCHANGE FLOOR

19. (SBU) Noting the August 27 floor is still in place on the Karachi Stock Exchange, Ross said that the longer the stock exchange floor remained in place, the harder it becomes to remove it. Removing the floor will certainly result in flight of foreign capital while foreign reserve stocks are low, but Ross said "there will be no right time" and it is necessary. The GOP continues to revise stock market support schemes but the IMF's view has been that the use of public funds is inappropriate. Ross noted that discussions on the floor removal have gone as far as possible at the staff level and the issue has now been elevated to the IMF's management for consideration of the GOP proposals. He noted that discussions on the issue would continue immediately after the EID holiday and could not confirm local press reports that the floor may be removed as early as December 15.

ELECTRICITY SUBSIDIES

110. (SBU) Concerning the removal of electricity subsidies, Ross said that the World Bank was working with the GOP on phasing them out. The proposal is that, beginning in January, consumers' bills will slowly increase month-by-month (2 to 4 percent) until the full subsidy is removed. However, the cabinet has not reached consensus yet on this approach. EconCounselor noted that this could present a great challenge to the GOP as public resentment continues to

increase as the electric bills rise while blackouts also increase. Ross agreed that the increasing electricity outages complicate the price increase commitments but hoped the USG would continue to encourage the GOP to adhere to its targets.

PATTERSON